

Date: February 7, 2013
To: Thomas J. Bonfield, City Manager
Through: Wanda S. Page, Deputy City Manager
From: Bertha T. Johnson, Director of Budget & Management Services
Subject: Interlocal Agreement for the Distribution of Sales Tax between the City of Durham and Durham County

Executive Summary

The current interlocal agreement for the distribution of sales tax between the City of Durham and Durham County expires on June 30, 2013. North Carolina General Statute (N.C.G.S.) Section 105-472 authorizes county boards of commissioners to decide how revenue from the local sales and use taxes are distributed to its municipalities. The board, by resolution adopted during the month of April of each year, determines which of the following two methods of distribution shall be in effect in the county during the next succeeding fiscal year:

- Per Capita Method – The net proceeds of the tax collected in a taxing county shall be distributed to that county and to the municipalities in the county on a per capita basis according to the total population of the taxing county, plus the total population of the municipalities in the county.
- Ad Valorem Method – The net proceeds of the tax collected in a taxing county shall be distributed to that county and the municipalities in the county in proportion to the total amount of ad valorem taxes levied by each on property having a tax situs in the taxing county during the fiscal year next preceding the distribution.

In lieu of Durham County changing the method of sales tax distribution, the City and County have agreed to enter into an interlocal agreement to continue the distribution of sales tax revenues between the City and County of Durham as in the previous agreement.

The current distribution methodology used in Durham County is the per capita method of distribution. Durham County has offered to renew the interlocal with the City of Durham with the following terms:

1. The sales tax will continue to be distributed by the state on a per capita basis between the County of Durham and the City of Durham.
2. The distribution ratio will remain the same at 42% for the City and 58% for the County.
3. This new agreement will remain in effect for five years: FY 2013-14 through FY 2017-18.

Recommendation

The Administration recommends that the City Council authorize the City Manager to execute a five year interlocal agreement with Durham County for the sharing of sales tax revenue.

Background

The City of Durham and Durham County have an interlocal agreement delineating how sales tax will be split between the two governments. The interlocal agreement expires on June 30th, 2013.

A 7.0% sales tax is imposed on most purchases in Durham County. The state retains 4.75% of the 7.0%; the additional 2.25% is distributed to the local governments.

The 2.25% Local Government Share is made up of:

- **Article 39: 1.0%;** distributed by point of sale, is the purest form of the Local Sales & Use Tax. Basically, any sale that occurs in a given county will result in the Article 39 portion returning to that county. Any refund identified as being from a specific county will have the Article 39 portion refunded from that county as well. Beginning with the October 2003 Collections, the Article 39 portion contains the “food tax” as instructed in G.S. 105-469.
- **Article 40: 0.5%;** distributed based upon a county’s population in relation to the state population total. A portion of the “food tax” is also included in Article. Article 40 is subject to an adjustment factor as identified in G.S. 105-486(b). This section contains the Article 40 portion of any refund.
- **Article 42: 0.5%;** previously distributed based upon a county’s population in relation to the state population total. Effective with the November 2009 collections distributed in January 2010, Article 42 tax is distributed on a point of sale basis. A portion of the “food tax” is also included in Article. The portion of the “food tax” included in Article 42 is subject to an adjustment factor as identified in G.S. 105-486(b). This section contains the Article 42 portion of any refund.
- **Article 46: 0.25% –** Article 46 allows an additional 0.25% local sales and use tax on transactions subject to the general State rate of sales and use tax pursuant to G.S. 105-164.4. Article 46 will be distributed based upon point of sale to the counties that enact this Article and is not shared with municipalities within these counties.
- **Article 44 Hold Harmless: –** Counties are required to hold eligible municipalities in each county harmless from the repeal of Article 44. Calculations are made to approximate the amount of Article 44 tax previously received by eligible municipalities. Effective October 1, 2008, the City Hold Harmless portion of the Distribution was calculated to provide eligible municipalities a replacement amount for the 0.25% of Article 44 that was repealed. Effective October 1, 2009, the calculation for the City Hold Harmless portion of the Distribution was changed to provide eligible municipalities a replacement amount for the final 0.25% of Article 44 that was repealed.

The current interlocal agreement between the City of Durham and Durham County for distribution of sales tax is effective through June 30, 2013. This agreement provides for a per capita split of 42% for the City and 58% for the County

The County is authorized to choose the allocation of local option sales tax (per capita vs. ad valorem) in April of each year. The new formula is effective from the beginning of the next fiscal year.

Durham County is proposing the following terms:

1. Sales Tax in Durham County will continue to be distributed by the state on a per capita basis.
2. The sharing ratio of all sales tax between the City of Durham and the County of Durham will be 42% to 58% respectively.
3. This agreement will remain in effect for five years: FY 2013-14 through FY 2017-18.

Issues and Analysis

North Carolina General Statute (N.C.G.S.) 105-472 authorizes county boards of commissioners to decide how revenue from the local sales and use taxes are distributed to its municipalities. By state statute, Counties chose the method of distribution of sales tax in every April counties can change the method of distributing local option sales tax revenues within the county from per capita to ad valorem or vice versa. The method chosen by the county board of commissioners determines the division of money among the county and municipal governments for the next year. Sales tax is a significant revenue source for the City representing 20.7% (\$36.7M) of the FY12-13 General Fund budget therefore, it is imperative that sales tax continue to be distributed on a per capital basis and that the City retains at least 42% of the distribution.

Alternatives

The City Council could elect to reject the terms offered by Durham County.

Financial Impact

The City's sales tax budget for FY12-13 is \$36.7M. In April 2013, if the County adopts a resolution to change the sales tax distribution method to ad valorem, the negative impact on the City is projected to be approximately \$1.3M.

SDBE

Due to the nature of this item, SDBE review is not applicable.